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BANKING IN MEXICO

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The development of banking in Mexico is one of the most important features of the Mexican economic improvement during the last thirty years.

Banking did not make its appearance here as a state institution but as the result of investments of foreign capital, attracted by the discovery of a great field for business, as soon as the country was able to establish peace firmly, after the tremendous struggles which followed the war for independence and lasted until the final triumph of the republican system.

In the ten years following the war with France, from 1870 to 1880, public credit was of no importance, and the financial relations between Mexico and Europe were practically nil; but during those years the construction of our big railroad systems was pushed very energetically, peace was assured, and the resources of the country became apparent to the eye of foreign money owners, always looking for sound and productive investments.

Several French and Mexican business men united to establish a bank of issue in Mexico City; and, supported by the government, which granted to them a liberal charter, founded the Mexican¹ National Bank. A few months later, Mexican and Spanish capitalists established the Mercantile Bank. The competition between these two institutions culminated in their merger, and the present National Bank of Mexico was thus created. Though not a state bank, this financial institution was authorized by the government, connected with it in many respects, subject to its supervision, and endowed with something very much resembling a monopoly of the right of issuing banknotes.

Nevertheless, the monopoly was not clearly defined in the charter; it was, besides, in opposition to the constitution of the country; no law existed restraining the freedom of issue, and very soon other banks appeared on the scene, such as the London and Mexico Bank,

which purchased an old and nearly forgotten charter granted to a bank which had never done anything serious in the way of business; the Nuevo Leon Bank, the Durango Bank and others, to which the Federal Government had granted charters, somewhat ignoring the not very clear nor legal monopoly granted to the National Bank.

A mortgage bank, also established by virtue of a charter from the government, began operations under the name of The International and Mortgage Bank.

There was no definite system for granting these charters; it was not even stated in a clear manner whether the government had a right to grant them, nor were the different charters founded upon the same principles of banking; in short, the whole matter was soon in a state of great confusion.

The National Bank had gradually developed its business, and through its different branches established in the principal towns of the country had contributed to the awakening of economic activities; the ground had been thus prepared for the business of banking and it was urgent to face the difficulties arising from the operations of other banks of issue, with a view to their settlement.

In 1897, the moment arrived to put order in the banking trade and a law was enacted by the government, with the necessary authority from Congress, and accepted by the National Bank, thereby forsaking its doubtful privileges.

The other existing banks also submitted to the law (in different ways) and the whole system was thus founded, as far as possible, upon a homogeneous basis.

The following statement of the principles which govern the law of 1897 will lead to its right understanding:

(1) Plurality in the monopoly, that is to say: the authority for doing a certain set of well defined banking operations, granted not to one bank only, but to many chartered banks, to the exclusion of any other institution.

(2) The banks must be operated under the form of limited companies duly organized in Mexico and subject to Mexican law. No foreign companies are authorized to do banking business pertaining to chartered banks.

(3) Legislative regulations for the management of the banks: sound economic principles are thereby enforced, not only morally and scientifically, but legally as well.

(4) Supervision by the state, the principal characteristics of which are the obligation of rendering certain statements intended for publication, and the submission to the intervention of the Secretary of the Treasury, acting as Comptroller of the Currency, by means of special delegates.

(5) The above regulations refer only to chartered banks, which are:

(a) Banks of issue, especially authorized to issue bank notes. No other banks, nor institutions, companies or individuals can make issues of this kind.

(b) Mortgage banks, the special feature of which is the issuing of mortgage bonds.

(c) Promotion banks, authorized to issue cash bonds.

Deposit banks, savings banks, trust companies and other banking institutions can be freely established without requiring any charter or previous authorization, be they Mexican or foreign. Following are the limitations concerning the institutions just referred to:

(1) They cannot issue banknotes nor establish in the country any branch or office for the redemption of notes issued abroad.

(2) They cannot use the word "bank" in designating themselves, except in the case of foreign banks, provided they are previously authorized by the Treasury Department.

(3) They are not subject to any special supervision from the government.

(4) They do not enjoy the reductions in taxation granted to the chartered banks.

Later on, a law was enacted, regulating the bonded warehouses, which are practically assimilated to credit institutions.

Under the law of 1897 about thirty-four banking institutions have been established, to wit: twenty-five banks of issue, three mortgage banks and six promotion banks.

We will now proceed to survey the field of operations of said banks as regards the most salient features.

Issue banks are authorized to issue bank notes, to accept deposits at sight and on term, and to make the investment of their capital and other funds in public securities and short-time loans.

As for notes, the issue may never exceed three times the face

value of the bank's stock, nor be superior to twice the amount of cash, less the total amount of the deposits payable at call.

Let us see how the Mexican issue banks have obeyed the legal ruling and, thereby, ascertain what is the guarantee in specie for their outstanding notes.

According to the official statements concerning issue banks, their cash holdings amounted in June 30, 1910, to 89,059,802.45 pesos (a peso being practically equal to fifty cents, American gold). This sum was represented by the following various species of currency:

Gold, coined	Pesos 53,690,870.00
Silver pesos	27,625,377.00
Fractional currency	5,705,834.83
Gold, bullion	2,037,720.62
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Total amount of cash holdings.....	89,059,802.45

As has been seen, in the above total the amount of gold coined and in bullion represents about five-eighths, and silver about three-eighths. These figures are very interesting as, besides showing beyond a doubt the soundness of the guarantee which stands behind the banknotes, they afford the assurance that the latter can be redeemed in gold, and this assurance is one of the strongest foundations for the stability of exchange.

Banks are permitted to put in circulation notes for twice the value of their cash holdings. Using the above figures we would have:

Twice the amount of cash holdings.....	Pesos 178,119,604.90
Less the amount of deposits on demand	67,826,271.91
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Authorized circulation	110,293,332.99

Now, the notes outstanding on said date (June 30th) amounted to pesos 112,160,663.00, this sum being about two millions greater than the authorized circulation. The reason of this difference is that the National Bank and the Nuevo Leon Bank, as we have said before, are not exactly subject to the prescriptions of the law and can issue notes for three times their cash holdings. Besides, the National and the London Bank are not obliged by their charters to hold a special reserve against their call deposits, and they only have

the reserve suggested by their own prudence, which is not always exactly fifty per cent of the deposits. Nevertheless, the metallic guarantee of our banks of issue is a very strong one.

For a full understanding of our system we must remark:

(1) Our system is that of "banking on assets," founded upon the "banking principle," being thus a very elastic one.

(2) This elasticity is increased by the fact that our notes are guaranteed by reserve funds in cash. It will be easy to see that we have not confused banking credit with public credit, and should a crisis occur in either, it does not follow that the other would of necessity experience a contraction.

(3) Metallic reserves are required, not only for the protection of the banknotes, but for that of the call deposits as well, as the danger for the public is the same, and perhaps greater in the case of the latter than in that of the former.

Under these wise principles business has grown, as can be seen from the following comparative statement of circulation:

Year	Banknotes outstanding.	Cash holdings.
1897	38,497,367.00.....	43,350,648.75
1898	46,471,650.75.....	34,819,723.93
1899	56,247,355.25.....	39,808,883.43
1900	62,657,714.50.....	53,107,694.67
1901	62,392,413.25.....	49,992,373.75
1902	72,890,235.50.....	53,147,288.30
1903	88,264,218.50.....	51,260,539.13
1904	83,540,440.00.....	56,245,838.69
1905	82,995,576.50.....	79,087,706.10
1906	93,597,868.50.....	63,695,882.24
1907	98,184,395.25.....	63,989,663.85
1908	89,659,571.00.....	64,910,541.18
1909	92,221,477.00.....	84,352,541.92
1910	112,160,663.00.....	89,059,802.45

The law does not consider the redemption of notes and the payment of deposits sufficiently assured by the possession only of cash reserves, and prescribes that the funds of the banks shall be invested in such a manner as to enable them to turn their investments into ready money at any time it becomes necessary. As we cannot go very deeply into this matter, we shall confine our examination to the principal regulations enacted with a view to reducing to a minimum the danger of defalcation.

It is forbidden to our banks of issue:

(1) To lend money upon a mortgage, except when the credit of the signers of obligations held by the bank is impaired, or when the Treasury Department gives its express consent.

(2) To make loans or to discount or negotiate notes or other paper running for more than six months.

(3) To discount notes or other commercial paper not guaranteed by at least two signatures of acknowledged solvency or by collateral security.

(4) To accept uncovered bills of exchange or drafts and to open credit accounts that cannot be closed at the bank's pleasure.

(5) To allow any single person or corporation to become indebted to them, either directly, indirectly or jointly, for amounts which, in the aggregate, exceed ten per cent of the paid-up capital of the bank.

(6) To acquire real estate, except such as is necessary for the carrying on of the business of the bank, etc.

These regulations have the very important effect of allowing banks to be provided with specie when needed to meet their obligations to the public. In case of a run on the bank or of a contraction of business, the nature of the assets will allow them to rediscount their bills, securities, etc., and thus to face the difficulty. We must say that in the history of Mexican banks of issue, and under the law of 1897, there has never been a run on any bank, and up to this writing, the circulation of banknotes has always been facilitated, in spite of their not being legal tender, by the high confidence bestowed upon them by the public; their redemption has invariably been effected without the least delay or difficulty, even in cases in which the public might have been distrustful. Our monetary system, which practically excludes the exportation of coined gold in the case of an adverse commercial balance, is not without influence in these facts.

As far as the true constitution of the assets can be known, it may be stated that the total of the reserve funds in cash, and of the assets readily realizable, exceeds the liabilities involving a public interest. The following figures will prove the last assertion:

ASSETS.

Cash	Pesos 89,059,802.45
(614)	

Loans, securities and bills readily realizable:

First class securities	55,832,029.59
Discounted bills	13,865,913.07
Loans	71,191,026.89
Loans on collateral securities, bonds, etc.....	41,245,500.02
Loans in current account	90,385,914.89
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	361,580,186.91

LIABILITIES.

(Only those involving a public interest.)

Deposits on call	Pesos 67,826,271.91
Deposits at term	58,026,027.36
Banknotes outstanding	112,160,663.00
Sundry creditors	45,971,688.52
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	283,984,650.79

The comparison between these two totals is evidence of the sound condition of the Mexican banks of issue.

The stock of these banks amounts to pesos 118,800,000.00 and their reserve funds, comprising those created by law and those created by the foresight of the banks amount to pesos 52,567,536.08.

Mortgage banks have not developed in the same manner as issue banks. We have but two institutions of this kind, and a third one will be established very soon. The first two do their business in the city of Mexico, and through branches, in all the country; the third will carry on banking in the State of Sonora.

The principal business of mortgage banks is the issue of bonds running for a long time, redeemable out of a special sinking fund twice a year, under the system of annuities and bearing interest payable semi-annually. The proceeds of the sale of these bonds must be devoted to the making of mortgage loans.

Special regulations are contained in the law, for the purpose of giving all security to the redemption of the bonds. Thus, the total amount of the bonds may never exceed the total of mortgage loans; the latter to be made under strictly fixed conditions in order to afford at any time a sound guarantee to the bondholders.

Banks of this kind do not enjoy any practical monopoly, neither in the nature of their investments (everybody being entitled to lend

money on mortgage) nor in the issuing of bonds, as all the limited companies, and specially the railroad companies, are authorized to issue mortgage bonds.

Such securities, as far as our banks are concerned, have proved to be an excellent investment for foreign capitalists, as the greatest part of the issues are owned by them.

The issue of bonds amounted on June 30, 1910, to pesos 44,904,-600.00 and have increased since then. The mortgage loans totaled pesos 46,872,918.47.

The prospect of these banks is a very bright one, as they can issue bonds for twenty times their paid up capital: as this amounts to pesos 10,000,000.00, they can carry their business to pesos 200,-000,000.00 even without any increase of their stock.

We give the name of promotion banks to certain institutions specially intended by the law to impart their help to agriculture, mining and manufacturing, by means of loans guaranteed according to a peculiar system which partakes of the mortgage and the pledge.

Promotion banks are authorized to issue cash bonds running from six months to three years; these bonds were created to afford opportunities for the investment of savings not yet intended for a definitive destination.

Unfortunately this kind of bank has not made great progress, perhaps owing to the influence of traditional causes closely linked to the solution of the very difficult question of agrarian credit.

The issue of bonds has only been made by one of these banks and in such a small amount that it is not worth while to mention it. The loans to cultivators or miners are practically of small importance. Two of these banks are in an unsatisfactory condition, doing but little business with correspondingly small profits. The other four, though in a thriving condition, are not properly promotion banks, as they do not carry on to a full extent the special business of this kind of institution; they are, rather, banking houses, doing a deposit, loan and exchange business, and financing other enterprises.

The most important promotion bank is the Mexican Central Bank, the individuality of which in our banking world will be set forth in the next and final chapter of this paper.

To bring this matter to an end we will state that the aggregate

of the promotion banks' stock amounts to pesos 47,800,000.00, their cash bonds to pesos 4,893,200.00; their loans for agricultural purposes to pesos 2,174,794.29, and their deposits to pesos 26,379,872.39.

The National Bank of Mexico—a bank of issue—and the Mexican Central Bank—a promotion bank—have a place of their own in our banking system.

The former is, for its capital, the importance of its notes outstanding and the bulk of its business, our principal banking institution. It has branches and agencies in all the capitals of the different states of the republic and covers the whole territory with its operations. Historically, it is the pioneer bank in Mexico and has educated all the country to the use of credit. Its relations with the government are of a very intimate character. It is entrusted with the payment of the different debts of the nation; it acts as a depository of the public funds; it concentrates the proceeds from the custom houses and other fiscal offices. Besides, it is a great rediscount bank which takes over the paper of the other banks when they are in need of money to meet their obligations.

The Mexican Central Bank is the most important of the promotion banks; but occupies a special position like a hyphen between all the issue banks established outside of the city of Mexico. It concentrates the notes of these banks and performs the services of a clearing house for them by exchanging their notes in the federal capital; it is verily a central bank as it acts as a regulator of all the issue banks of the different states of the republic. It has, besides, obligated itself to support in different ways the before mentioned banks in case of difficulty. In short, the Mexican Central Bank is, in many of its features, a result of the co-operation between the issue banks.

Such is the Mexican banking system, which may be concisely defined by saying that it is a plural system of privileged institutions under government inspection, whose business is regulated by the operation of two greater banks.